

BEFORE
THE PUBLIC SERVICE COMMISSION OF
SOUTH CAROLINA
DOCKET NO. 93-750-C - ORDER NO. 94-400 *✓*
MAY 6, 1994

IN RE: Request of Pond Branch Telephone)	ORDER APPROVING
Company for Approval of Optional)	EXTENDED AREA
Extended Area Calling Plan.)	CALLING PLAN AND
)	RATE OF RETURN
)	ON RATE BASE

I.

INTRODUCTION

This matter comes before the Public Service Commission of South Carolina (the Commission) by way of a tariff filing on December 6, 1993, by Pond Branch Telephone Company (Pond Branch or the Company) for approval of revisions to its General Subscriber Service Tariff. The purpose of the filing is to introduce an optional extended area calling plan known as "Pond Branch Plus +" (the Plan).

By letter dated December 21, 1993, the Commission's Executive Director instructed Pond Branch to publish, one time, a prepared Notice of Filing in newspapers of general circulation in the area affected by the Company's tariff filing. The Notice of Filing indicated the nature of Pond Branch's tariff filing and advised all interested parties of the manner and time in which to file the appropriate pleadings for participation in this proceeding. Pond Branch submitted an affidavit indicating that it had complied with these instructions. Petitions to Intervene were filed by the

Consumer Advocate for the State of South Carolina (the Consumer Advocate), the South Carolina Public Communications Association (SCPCA), and AT&T Communications of the Southern States, Inc. (AT&T).

On February 7, 1994, a public hearing concerning the matters asserted in the Company's tariff filing was commenced in the Commission's Hearing Room. The hearing was continued on February 25, 1994, for the purpose of taking testimony relative to the Company's rate of return. The Honorable Henry G. Yonce, Chairman, presided over the proceedings. The Company was represented by M. John Bowen, Jr., Esquire; the Consumer Advocate was represented by Elliott F. Elam, Jr., Esquire; the SCPCA was represented by John F. Beach, Esquire; AT&T was represented by Francis P. Mood, Esquire; and the Commission Staff was represented by Florence P. Belser, Staff Counsel.

During the hearing, Pond Branch presented the testimony of Luther E. Kneece, Bruce Schoonover, and Dr. William E. Avera. The Consumer Advocate presented the testimony of Dr. John B. Legler. AT&T presented the testimony of Mike Guedel. Gary E. Walsh testified on behalf of the Commission Staff. Following the hearing, the Commission allowed all parties the opportunity to file a written brief in this case.

The Commission will consider the issues of approval of the "Pond Branch Plus +" Plan and of setting a rate of return separately. Based on the evidence presented at the hearing, the tariff filing of the Company, and the applicable law, the Commission makes the following findings of fact and conclusions of

law:

II.

THE "POND BRANCH PLUS +" PLAN

A. FINDINGS OF FACT

1. The "Pond Branch Plus +" Plan filed by Pond Branch Telephone Company is an optional 40-mile, 7-digit calling plan. Residential and business customers subscribing to "Pond Branch Plus +" will be able to make 7-digit calls to an area extending 40 miles from the Pelion access tandem. The "Pond Branch Plus +" Plan has two important components, the Basic Service Area (BSA) and the Expanded Service Area (ESA). The BSA is an area in which telephone service is furnished under a specific schedule of exchange rates and coincides with the current calling scope. The ESA is an area beyond the subscriber's BSA and within the Columbia Local Access and Transport Area (LATA) and within 40 miles of the Pelion access tandem.

2. The rates for "Pond Branch Plus +" depend upon which "option" is selected by the customer. Each of the new residential options has a monthly line charge of \$8.00. Under Residential Option 1, all calls within the BSA are billed at \$0.02 per minute during peak hours and \$0.01 per minute during off peak hours with a cap on usage charges of \$15.00 for calls within the BSA, and calls within the ESA are billed at \$0.11 per minute during peak hours and \$0.055 per minute during off-peak hours. Under Residential Option 2, subscribers pay the monthly line charge of \$8.00 and a subscription fee of \$2.00 and receive a 20% discount on BSA and ESA calls. Option 2 also has a \$15.00 usage charge cap on BSA calls.

Under Residential Option 3, the residential subscriber pays the monthly line charge and a subscription fee of \$30.00 which enables the subscriber to make unlimited calls within both the BSA and the ESA.

Business subscribers to "Pond Branch Plus +" will pay the current tariffed monthly line charge rate of \$19.00 per line. Under Business Option 1, the subscriber will pay the monthly line charge plus \$0.02 per minute during peak hours and \$0.01 per minute for off peak hours for calls made within the BSA, and ESA calls will be charged \$0.11 per minute for peak hour calls and \$0.055 per minute for off peak hour calls. Under Business Option 2, a subscription fee of \$3.00 will give the subscriber a 20% discount on BSA and ESA calls. Under Business Option 3, the subscriber pays the monthly line charge and a subscription fee of \$20.00 and receives a 50% discount on BSA and ESA calls with a usage cap of \$20.00 for calls within the BSA. "Pond Branch Plus +" does not afford business subscribers a flat rate option.

3. Luther E. Kneece, General Manager of Pond Branch Telephone Company, Inc. explained the "Pond Branch Plus +" Plan at the hearing. According to Mr. Kneece, "Pond Branch Plus +" was proposed in response to the needs of the Pond Branch customers. Mr. Kneece stated that Pond Branch has received inquiries, as well as complaints, concerning the customers' desires to communicate locally with adjacent exchanges. Mr. Kneece stated that most of the Pond Branch subscribers rely on jobs outside the Pond Branch service area. TR. Vol. 1, p. 45. Mr. Kneece stated that several towns in the Pond Branch service area serve as "bedroom

communities" to the larger urban areas of Columbia, Lexington, and Orangeburg. The Pond Branch customers share a community-of-interest with the larger metropolitan areas and desire reasonably priced communication services with these areas. TR. Vol. 1, p. 45.

Mr. Kneece also stated that Pond Branch has continued to experience growth associated with its proximity to the larger Columbia/Lexington area and the popularity of Lake Murray. TR. Vol. 1, p. 44. Further, Mr. Kneece testified that the expanded calling area will assist in removing artificial barriers to economic growth, help land development, which should improve the tax base, and help maintain the Pond Branch service territory as an economically viable area. TR. Vol. 1, p. 46. Additionally, the "Pond Branch Plus +" Plan will assist the Pond Branch customers in effectively reaching vital services related to medical needs, government agencies, advanced education, social activities, and shopping centers on which the Pond Branch customers rely, but which are located outside the Pond Branch service area. TR. Vol. 1, pp. 45-46.

Mr. Kneece further testified that the optional nature of the Plan would allow those subscribers who would not benefit from the Plan to continue with their current service. TR. Vol. 1, p. 51. Also, Mr. Kneece stated that the Plan would not result in a subscriber paying more for service under the Plan. TR. Vol. 1, p. 51. Mr. Kneece also stated that Pond Branch's business office is prepared to assist subscribers in deciding which option best suits their needs. TR. Vol. 1, p. 52, 58. Mr. Kneece further testified

that a subscriber could try the Plan, and if he or she is not satisfied with the plan, the subscriber could return to his or her old service at no charge. TR. Vol. 1, p. 61.

Mr. Kneese testified that AT&T had not, as of the date of this hearing, filed an order with Pond Branch to open AT&T's carrier code which would allow 10XXX dialing within the LATA. TR. Vol. 1, pp. 81-82, 89. According to Mr. Kneese, the failure of AT&T to request that Pond Branch open its network to the AT&T access code prevented Pond Branch customers from making intraLATA calls using AT&T. TR. Vol. 1, pp. 81-82, 89.

Mr. Kneese also testified that a goal in creating the Plan was that the Plan would be revenue neutral. However, Mr. Kneese stated that it is anticipated that the Plan will reduce the earnings of Pond Branch by approximately \$206,000. TR. Vol. 1, p. 52. Mr. Kneese stated that Pond Branch does not anticipate the need for any rate adjustments based on that projected loss of revenue, and further stated on cross-examination that Pond Branch would not use any losses which it incurs as a result of offering the Plan to justify a local rate increase. TR. Vol. 1, p. 59.

4. Several Pond Branch subscribers appeared at the hearing to offer testimony about the "Pond Branch Plus +" Plan. Most of the public witnesses offered their support of the Plan. One public witness testified that the Plan would not meet her needs, but she acknowledged that the plan would benefit those subscribers who made many calls. TR. Vol. 1, pp. 13-14. The public witnesses also offered testimony that the community of interest of the Pond Branch subscribers exceeds the boundaries of the Pond Branch service area.

5. Gary E. Walsh, Assistant Director of the Utilities Division of the South Carolina Public Service Commission, testified on behalf of the Commission Staff. Mr. Walsh testified that since 1987, he has been responsible for the review and preparation of cost studies and community-of-interest studies involving a tremendous number of Extended Area Service (EAS) requests. According to Mr. Walsh, EAS requests generally have similar characteristics, in that a small community or pocket of customers request flat rated toll-free calling between their community and a larger community. Generally, when the Commission has ordered that a ballot process be conducted, the requests fail due to lack of interest for calling from the larger community back to the smaller community. TR. Vol. 2, pp. 44-47.

Mr. Walsh testified that Pond Branch has experienced more EAS requests and pressure than the majority of local exchange companies in the state. Mr. Walsh offered that this increased EAS pressure is due to the close proximity of the Pond Branch service area to Lexington and Columbia. Mr. Walsh also stated that this EAS pressure is compounded by the fact that many individuals have recreational properties in the Pond Branch service area while residing in Lexington or Columbia. TR. Vol. 2, p. 47. Mr. Walsh testified that the EAS requests have not been successful because there was very little interest in calling from the larger areas back into the Pond Branch area. TR. Vol. 2, p. 53. Mr. Walsh also offered that the Plan should be of great benefit to the Pond Branch subscribers as the Plan will benefit those customers who have a large volume of calling as well as those subscribers who make very

few calls. TR. Vol. 2, pp. 49-50,52.

6. Mike Guedel, Manager of Network Services Division of AT&T, testified on behalf of AT&T. Mr. Guedel testified that approval of the "Pond Branch Plus +" Plan would eliminate intraLATA competition since the cost of an "Pond Branch Plus +" call would be less than the access charges charged the interexchange carriers. TR. Vol. 2, p. 24. Mr. Guedel also testified that the "Pond Branch Plus +" is based upon discriminatory pricing of switched access service. Mr. Guedel testified that AT&T is not opposed to the toll relief proposed by Pond Branch but that such relief should not be at the expense of customer choice. TR. Vol. 2, p. 25. Mr. Guedel suggests that one way the Commission could accomplish the granting of toll relief while maintaining competition would be to eliminate originating and terminating carrier common line charges. TR. Vol. 2, pp. 25-26. Mr. Guedel also suggests that the Commission should make the arrangements embodied in the Area Calling Plan Principles Agreement (ACP Principles Agreement) available to providers of toll services. TR. Vol. 2, p. 25. Mr. Guedel stated that, after learning in the hearing that AT&T had not requested that its 10XXX access code be unblocked by Pond Branch, that AT&T had begun the necessary procedure to unblock its access number in the Pond Branch service area.

7. Bruce Schoonover, Executive Vice President of John Staurulakis, Inc., also testified on behalf of Pond Branch. Mr. Schoonover stated that the purpose of his testimony was to respond to statements made by Mr. Guedel relating to the "Pond Branch Plus +" Plan and the Area Calling Plan Principles Agreement. TR. Vol. 2,

p. 65. Mr. Schoonover testified that the ACP Principles Agreement is a local settlement mechanism for LECs. TR. Vol. 2, p. 69. According to Mr. Schoonover, the ACP Principles Agreement resulted from concerns over "depooling" and that the ACP Principles Agreement followed as an effort to provide financial stability to the LECs in the "depooling" environment with the increased pressure to provide low cost expanded local calling alternatives. TR. Vol. 2, pp. 67-69. Mr. Schoonover also testified that the carrier common line charge is an access rate element approved by the Commission to allow LECs to recover their access related costs from toll providers and IXC's. He also stated that access charges were never intended to be imputed on a local service offering and that he would not recommend that Pond Branch agree to waive the carrier common line charge as suggested by AT&T. TR. Vol. 2, p. 73.

8. The SCPCA and Pond Branch reached a Stipulation in which Pond Branch agreed to amend its tariff so that the Pond Branch tariff is consistent with Southern Bell's Area Plus filing regarding the treatment of COCOTs. Specifically, Pond Branch's amended tariff no longer excludes COCOTs from the "Pond Branch Plus +" service thereby allowing COCOTs to participate in the "Pond Branch Plus +" Plan on the same basis as Pond Branch's other business customers.

B. CONCLUSIONS OF LAW

1. Pond Branch is a utility within the meaning of of S.C. Code Ann. §58-9-10(6) (1976). Consequently, Pond Branch's intrastate operations are subject to the jurisdiction of this Commission.

2. The Commission concludes that the "Pond Branch Plus +" Plan should be approved. The testimony from the hearing supports the position that the community of interest of Pond Branch subscribers far exceeds the boundaries of the Pond Branch service area. It is clear from the testimony that much of the Pond Branch service area has become integrated with larger urban areas which is separated by toll borders. Approval of the "Pond Branch Plus +" Plan will benefit the Pond Branch subscribers by integrating the service area with nearby metropolitan areas. The Commission concludes that the benefits of the "Pond Branch Plus +" Plan as filed by Pond Branch and as supported by the testimony of Kneece, Schoonover, Walsh, and the public witnesses far outweigh the potential problems cited by the intervenors in this Docket. According to the testimony, the scope of the Plan should cover the EAS requests formerly before the Commission. Further, the Plan is an optional plan so only those customers who wish to participate in the plan would do so. Therefore, the Commission concludes that the "Pond Branch Plus +" Plan should be approved, as amended herein and by the Stipulation between Pond Branch and the SCPCA, and for the reasons stated above, the Commission determines that the Plan is in the public interest.

3. In approving the "Pond Branch Plus +" Plan, the Commission has exercised its power and discretion granted by S.C. Code Ann. §58-3-140 and §58-9-250 to reclassify this calling traffic as local service. In approving the Plan, the Commission has considered the potential impact which the Plan may have to encourage land development in the area, the positive impact to subscribers in ease

of use and in reducing rates, the optional nature of the plan, and the minimal impact on the revenues of Pond Branch so that the benefits of the Plan will be afforded with no increase in rates for local or other service.

S.C. Code Ann. §58-3-140(A) (Supp. 1993) designates that this Commission is vested with power and jurisdiction to supervise and regulate the rates and service of every public utility in this State and to fix just and reasonable standards, classifications, regulations, practices, and measurements of service to be furnished, imposed, or observed, and followed by every public utility in this State." S.C. Code Ann. §58-3-140 (A) (Supp. 1993) (emphasis added).

Additionally, although telephone utilities may not grant unreasonable preferences or advantages, "[s]ubject to the approval of the Commission, ..., telephone utilities may establish classifications of rates and services and such classifications may take into account the conditions and circumstances surrounding the service, such as time when used, the purpose for which used, the demand upon plant facilities, the value of the service rendered or any other reasonable consideration. The Commission may determine any question arising under this section." S.C. Code Ann. §58-9-250 (1976) (emphasis added).

Also, AT&T has specifically agreed that those offerings which are filed under the toll sections of the General Subscriber Service Tariff (GSST) are toll services. See, Exhibit B to May 10, 1993, Stipulation and Agreement on IntraLATA Competition attached to Order No. 93-462 (June 3, 1993). Here, Pond Branch filed its "Pond

Branch Plus +" Plan under the local, rather than toll, section of its GSST. Consequently, with approval as granted herein, the "Pond Branch Plus +" Plan is a local service.

4. The Commission believes that the "Pond Branch Plus +" Plan will benefit Pond Branch subscribers and therefore approval of the Plan is in the public interest. Since the Plan is optional, it will serve those subscribers who wish to utilize the plan but will not burden those subscribers who either have no desire or who have no need to use the Plan.

5. Further, the Commission is not persuaded by AT&T's argument that approval of the Plan will eliminate intraLATA competition. While the Commission notes with particular interest that prior to the hearing AT&T had not requested that its access code be opened in the Pond Branch service area, the Commission concludes that the "Pond Branch Plus +" Plan does not preclude AT&T from competing for intraLATA service. All Pond Branch subscribers must still select an interexchange carrier to complete intraLATA calls which are not originated or terminated within the 40-mile radius of the Pelion access tandem. Furthermore, all Pond Branch customers can still access the interexchange carrier of their choice to carry a call within the Pond Branch service area, provided the IXC has requested that its access code be activated.

6. The Commission notes that the tariff filed by Pond Branch does not include a usage cap of \$20.00 for calls within the BSA under Business Option 3 as indicated by the testimony and exhibits of Mr. Kneece. The Commission approves the \$20.00 usage cap for calls within the BSA under Business Option 3. Pond Branch shall

file a revision to its tariff reflecting this usage cap.

III.

RATE OF RETURN

A. FINDINGS OF FACT

1. In Docket No. 93-401-C, the Commission authorized a rate of return on rate base of 13.00% for Pond Branch. The Commission further stated that the issue of rate of return could be raised in the expanded area calling plan case. The Consumer Advocate served notice that it would raise the rate of return issue in this Docket, with special emphasis on rate of return on common equity.

2. As to the rate of return issue on common equity and rate base, the Consumer Advocate presented Dr. John B. Legler as its witness. Dr. Legler testified that a fair and reasonable rate of return on rate base for Pond Branch is 10.25%. TR. Vol. 3, p. 46. Dr. Legler arrived at this estimate by using a capital structure consisting of 40.32% debt and 59.68% common equity, an embedded cost of debt of 7.66%, and a cost of common equity of 12.00%. TR. Vol. 3, p. 46. Dr. Legler testified that he obtained his cost of common equity by applying the standard financial models to a group of Bell Regional Holding Companies, and to a group of publicly traded larger independent telephone companies. TR. Vol. 3 p. 53. Dr. Legler testified that he judged this group of larger publicly traded companies to be comparable to Pond Branch, and he concluded that the cost of common equity would be in the range of 11.0 to 12.0 percent. TR. Vol. 3, p. 53.

Dr. Legler also stated that "it is almost impossible to select a sample of utilities which is strictly comparable to the company

(Pond Branch) being reviewed." TR. Vol. 3, p. 27.

3. Pond Branch presented Dr. William E. Avera as a witness on the rate of return on common equity and rate base. Dr. Avera testified that the 13.00% rate of return on rate base approved by the Commission in Docket No. 93-401-C is a fair and reasonable return for Pond Branch Telephone Company. TR. Vol. 3, p. 81. Dr. Avera disagreed with the approach Dr. Legler used in calculating a rate of return. TR. Vol. 3, p. 104. Dr. Avera testified that if one approached the rate of return issue as Dr. Legler did - i.e. by starting with large, publicly traded companies - then certain adjustments must be made in the cost of capital and in the capital structure to make the comparison to a company such as Pond Branch. TR. Vol. 3, p. 104. Dr. Avera testified that adjustments must be made to account for the additional risk that a small closely held company faces as opposed to a large publicly traded company. TR. Vol. 3, p. 105. To account for this risk factor, Dr. Avera added an adjustment, or risk premium, to Dr. Legler's cost of common equity estimates. Dr. Avera stated that if one uses the returns on equity of the large companies, as utilized by Dr. Legler, then one must increase the returns on equity significantly to adjust for this risk factor. TR. Vol. 3, pp 106-107.

Dr. Avera also testified that the size of a company has important implications with respect to risks and, in turn, to the cost of equity. TR. Vol. 3, p. 83. According to Dr. Avera, all else being equal, smaller firms are more risky than larger ones due to their lack of diversification and absence of financial resiliency. TR. Vol. 3, p. 83. Dr. Avera stated that the large

telephone companies in Dr. Legler's samples are able to mitigate many risks through geographic diversification but that Pond Branch is wholly exposed to the risks associated with economic conditions, natural disasters, demographics, and other factors which could impact a small, concentrated service area. TR. Vol. 3, p. 83. Additionally, small companies such as Pond Branch do not have the ability to raise additional capital with the relatively little difficulty that the larger companies have. TR. Vol. 3, p. 83. According to Dr. Avera, Dr. Legler's estimate of 12% cost of common equity does not take into account Pond Branch's small size, lack of diversification, and illiquidity. Dr. Avera concluded that, Dr. Legler's recommendation of 12% is well below the cost of common equity for Pond Branch, and that Dr. Legler's recommended 10.25% return on rate base is not a fair and reasonable overall rate of return. TR. Vol. 3., p. 94.

Dr. Avera testified that even accepting Dr. Legler's 11 to 12% range for the cost of equity for larger, publicly trade companies, that the cost of equity for a company such as Pond Branch would be in the neighborhood of 16 to 17%. TR. Vol. 3, p. 92. Dr. Avera testified that combining his range of reasonable capital structure ratios with the respective costs of equity that a reasonable overall rate of return for Pond Branch would be from 12.66 to 13.53%. TR. Vol. 3, p. 95, 108.

4. Mr. Walsh testified that the Commission has used the 24 to 25 small LECs in South Carolina as a comparison group for companies such as Pond Branch rather than trying to ascertain a group of publicly traded companies for comparison purposes as Drs. Legler

and Avera attempted to do. TR. Vol. 3, p. 167.

B. CONCLUSIONS OF LAW

1. Pond Branch is a small, independent utility. It is a closely held corporation whose stock is not publicly traded. The Commission believes that the capital structure and cost of debt of Pond Branch as of December 31, 1992, is reasonable.

2. The Commission recognizes certain issues which must be considered when attempting to apply the cost of equity concept to any small regulated company in the same manner that it is applied within rate cases for major regulated companies. First, there is the difficulty involved in developing meaningful and appropriate cost of equity estimates for the small regulated companies. The Commission recognizes that it is impossible to determine an exact value for the cost of equity of a small utility such as Pond Branch. Secondly, there is the concern regarding the increased costs of regulation which result during the proceedings.

As most small regulated companies, such as Pond Branch, are not traded on major stock exchanges and are often largely closely held, the tools available to financial analysts, such as Drs. Legler and Avera, to estimate the cost of equity rely on market data available on comparable companies. Dr. Legler acknowledged that it is almost impossible to select a sample of companies which would be comparable to Pond Branch, and Dr. Avera's testimony also demonstrated the difficulty of selecting a comparable group of companies. To apply the results of a sample estimate based on much larger companies to a small regulated utility requires the assumption that the business risks and financial risks of the large

companies are similar in type and magnitude to those of the small company. The accuracy of such an assumption is often arguable. It is certainly arguable in this case.

To compensate for differences in business risk between the large companies of his sample and Pond Branch, Dr. Legler selected the upper end of his range. Dr. Avera did not attempt to use a sample of comparable telephone companies, but used the estimates of Dr. Legler as the beginning point, or benchmark, of his cost of equity values. Dr. Avera then added a "risk premium" of 5.1% to Dr. Legler's estimates, based on historical returns for a sample of Small Company Stocks contained within studies conducted by Ibbotson and Associates.

The Commission perceives problems with both Dr. Legler's and Dr. Avera's approaches in attempting to estimate the cost of equity for Pond Branch in this case. The results of the cost of equity estimates presented to the Commission range from Dr. Legler's low estimate of 11.00% to a high of 17.00% presented by Dr. Avera, or a very broad range of 600 basis points. This broad range is indicative of the numerous problems associated with trying to determine a reliable and fair cost of equity estimate for a small regulated utility such as Pond Branch. Such a broad range of estimates does not give the Commission a clear indication of an appropriate cost of equity value.

Given the broad range of cost of equity estimates presented within this case, the Commission finds that there is not a sufficient improvement in the accuracy of the cost of capital and rate of return on rate base value for Pond Branch to justify

treating the cost of equity of Pond Branch, or any such small regulated utility, in a manner consistent with the regulatory treatment for the larger utilities which have available appropriate market data and comparable risk companies for purposes of deriving reasonable cost of equity estimates. Therefore, the Commission will continue to rely on the concept of rate of return on rate base as the basis for determining the revenue requirements for Pond Branch. The Commission will continue to use the other small LEC's in South Carolina as a comparison group for companies such as Pond Branch.

The Commission's reliance upon the rate of return on rate base does not mean that the parties of record in a given rate proceeding related to a small regulated utility such as Pond Branch are prohibited from submitting information regarding the cost of equity. The Commission will give such information the weight within its decision process that it warrants at that point in time. However, the Commission would like to point out that any party choosing to make the cost of equity of a small regulated utility an issue within the regulatory process is adding to the cost of regulation. The utilization of external cost of equity witnesses such as Drs. Legler and Avera within the Pond Branch case added substantially to regulatory costs. In the Pond Branch case, the Company had to employ a witness at a cost of between \$10,000 and \$15,000, which is only one of the additional costs eligible to be borne by ratepayers. Other related costs include expenditures for additional financial analysts and legal fees. On the basis of the results of the Pond Branch case, the Commission believes that the increased regulatory costs of considering the cost of equity

component of the overall rate of return for small regulated companies such as Pond Branch are not offset by a sufficient increase in the accuracy in the rate of return estimate. The Commission would suggest that should any party choose to submit information concerning the cost of equity for any small regulated utility in future rate cases that they do so on a selective basis to minimize the potential burden on ratepayers. The Commission does not wish to see regulatory costs become an undue burden for such small utilities and their ratepayers.

4. Based upon the evidence, the Commission determines that a fair and reasonable return on rate base of 12.64% should be authorized for Pond Branch to set rates. The Commission finds that the approaches of both Dr. Legler and Dr. Avera for estimating the cost of equity of Pond Branch have apparent weaknesses which reflect the difficulty of developing a fair and reasonable cost of equity estimate for small regulated utilities. Despite such problems with the cost of equity analyses, Dr. Avera's analysis supports a rate of return on rate base between 12.64% and 13.24% on rate base. The Commission agrees with Dr. Avera that the business risk and the financial risk of Pond Branch exceeds that of the sample utilized by Dr. Legler. The risk premium recommended by Dr. Avera, which more adequately reflects this additional risk, is more appropriate than the premium applied by Dr. Legler to his sample of companies. The rate of return on rate base for Pond Branch falls within a range of 12.64% and 13.24% when considering the cost of equity estimates of Dr. Avera along with the actual capital structure and cost of debt of Pond Branch as of December 31, 1992.

For purposes of this proceeding, the Commission chooses to set rates for Pond Branch at 12.64% on rate base.

5. A rate of return on rate base of 12.64% will allow the Company to meet its statutory requirements to provide adequate, efficient, and reasonable service, will provide a return to the Company's owners commensurate with returns on investments in other enterprises with corresponding rates, and will assure confidence in the financial integrity of the Company.

6. This authorized rate of return will require Pond Branch to file revised tariffs which will lower rates prospectively by \$67,096. Pond Branch shall file revised tariffs to reflect the findings of this Order within thirty (30) days of receipt of this Order.

IT IS THEREFORE ORDERED THAT:

1. The "Pond Branch Plus +" Plan, as amended by the Stipulation with the SCPCA and as stated herein, is approved.

2. Pond Branch shall maintain records which will show the revenue effect of Pond Branch's participation in the Area Calling Plan Principles Agreement on its revenue requirement and the revenue requirement of other LECs which terminate Area Calling Plan-type calls in Pond Branch's service area. The records shall also include the amount of terminating carrier common line charges avoided as a result of the Area Calling Plan Principles Agreement.

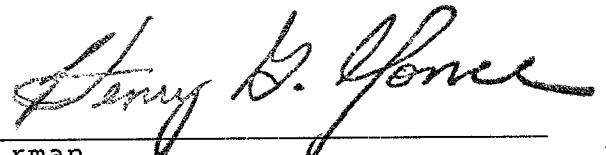
3. Pond Branch is hereby granted the opportunity to earn an authorized rate of return of 12.64% on its South Carolina combined rate base.

4. Pond Branch shall file revised tariffs to reflect the

findings of this Order within thirty (30) days of receipt of this Order.

5. This Order shall remain in full force and effect until further Order of the Commission.

BY ORDER OF THE COMMISSION:


Chairman

ATTEST:


Executive Director

(SEAL)